

VZCZCXRO7070
RR RUEHPT
DE RUEHBY #0511/01 1520646
ZNY CCCCC ZZH
R 010646Z JUN 09
FM AMEMBASSY CANBERRA
TO RUEHC/SECSTATE WASHDC 1559
INFO RUEHOT/AMEMBASSY OTTAWA 2336
RUEHWL/AMEMBASSY WELLINGTON 5802
RUEHGP/AMEMBASSY SINGAPORE 1739
RUEHBJ/AMEMBASSY BEIJING 9487
RUEHKO/AMEMBASSY TOKYO 3556
RUEHDN/AMCONSUL SYDNEY 4606
RUEHBN/AMCONSUL MELBOURNE 6381
RUEHPT/AMCONSUL PERTH 4645
RULSDMK/DEPT OF TRANSPORTATION WASHINGTON DC

C O N F I D E N T I A L SECTION 01 OF 03 CANBERRA 000511

SIPDIS

STATE FOR EEB/TRA, EAP/ANP

E.O. 12958: DECL: 06/01/2014

TAGS: [EAIR](#) [ECON](#) [AS](#)

SUBJECT: GFC, H1N1, AND OPEN SKIES, OH MY! A LOOK AT
AUSTRALIA,S TOP TWO AIRLINES

Classified By: Acting Econ Couns W Albright, reasons 1.4 b, d

¶1. (SBU) Summary. The Australian civil aviation industry has not escaped the economic slowdown brought on by the intensified global financial crisis. Qantas remains the heavyweight in the Australian aviation arena, but its share of the domestic market is slipping and is now down to around 60%. Top rival Virgin Blue recently released figures showing continued domestic traffic growth into early 2009. Both Qantas and Virgin Blue both claim to be coping reasonably well with the economic slowdown. Both have reduced capacity on some routes, and are looking at reducing labor forces for the short term. With V Australia's entry, increased competition has made the Australia-California routes "a bloodbath." Qantas and Virgin Blue see the potential entry of Delta into the trans-Pacific market very differently. H1N1 influenza remains a wild card for Australian aviation. End summary.

STATE OF QANTAS

¶2. (SBU) Econoff met with Qantas government affairs manger Jane McKeon to discuss how Qantas was managing with the effects of Open Skies, the economic downturn, and H1N1 influenza's emergence. First, some numbers. Qantas' most recent half-year profits before taxes were down 68% to A\$288 million (roughly US\$230 million at current exchange rates) - down, but still profitable. For the full year, they are projecting profits of A\$100-200 million, well down from the original estimates of A\$500 million. Qantas has already shed around 1750 jobs. McKeon said that soon Qantas would let go around 500 employees, mostly managers. In addition, there are around 1250 line positions marked for reduction. To a significant extent, Qantas is achieving this thru attrition, and by asking employees to take extended leave they have accrued or to work half-time; most of those people will not be fired. Qantas has cancelled dozens of less-profitable domestic routes, and has consolidated the number of flights on some segments. It is deferring capital expenditure, and retiring older and less efficient aircraft. McKeon said Boeing's delay on delivering 787s was a blessing in disguise; Qantas has deferred some other deliveries until conditions improve.

¶3. (SBU) Domestically, McKeon said the down market was holding up well, with a shift in traffic from Qantas to low-cost subsidiary Jetstar. Qantas has been running promotions to sell seats, and redemptions of frequent flyer miles are up significantly. However, Qantas' international business is hurting. Premium cabin class revenues are down

as much as 40% on some routes, and across Qantas, international network are down 20%. McKeon acknowledged that Virgin Blue's US service (under the name V Australia) was hurting Qantas - but the global financial crisis is hurting worse.

14. (SBU) Beyond June, Qantas is taking a wait-and-see attitude, but still intends to advance their strategic priorities, which include continuing their two-brand (Qantas and low-cost subsidiary JetStar) strategy, emphasizing product enhancement, and improving fleet efficiency. McKeon said she hoped GOA predictions of a return to growth in late 2009 would hold true, and indicated Qantas were cautiously optimistic. But, she added, H1N1 influenza remains an unpredictable factor. To date, she said Qantas had seen no impact on their operations internationally or domestically from the outbreak. But now that H1N1 appears to be establishing itself in Australia (over 300 cases confirmed as of June 1, but no deaths), they are watching the developments closely. McKeon thought as long as the flu remained mild, the impact on travel would not be unbearable.

VIRGIN BLUE COPING

15. (SBU) Virgin Blue's government affairs general manager Tony Wheelens told econoff that so far Virgin Blue is coping with the downturn fairly well. Traffic started to drop in October 2008, and Virgin Blue began to reduce capacity on some domestic routes. Rather than leave these aircraft idle, Virgin Blue accelerated existing plans to launch new services to Indonesia, Papua New Guinea, and the Solomons, and have

CANBERRA 00000511 002 OF 003

expanded operations to New Zealand and Fiji. Wheelens said Virgin Blue was trying to avoid laying off people, and pilots were doing job shares and taking long service leave. Wheelens noted the tremendous challenge Virgin Blue had faced in hiring qualified people during the recent boom economy and said they didn't want to make short-sighted decisions that would leave them scrambling when the recovery began. In April, Virgin Blue decided to make some cuts, cutting 400 jobs (mostly through attrition), and standing down some older aircraft.

16. (SBU) Wheelens observed wryly that February 2009 was not the best time to launch new services from Australia to the United States, and the potential threat from H1N1 is still a possible complicating factor. Virgin Blue subsidiary V Australia began Sydney to Los Angeles services in February, Richard Branson coming to Sydney for a characteristically splashy celebrity-studded launch party. Since then, they have begun Brisbane-LA flights, and still plan to start Melbourne-LA flights in September or October. Competition across the Pacific among Qantas (and partner American Airlines), United (and partner Air New Zealand) and V Australia was "a bloodbath" in Wheelens' words. There are very attractive fares between Australia/New Zealand and the US right now, and Wheelens said that Australia-California fares were down 40% (a number echoed by the GOA's Stephen Borthwick). V Australia was off to a good start, per Wheelens - 60% load factors, although yields were "ordinary" (that is, not great) on the Pacific routes - a problem all carriers around the world are facing, he added.

THE DELTA FACTOR

17. (SBU) Although they have not contacted Embassy Canberra, Delta Airlines executives have been quoted in the Australian media as saying they will be coming to Australia starting in July and will be a "disaster" for Qantas. Qantas' McKeon said Delta's head of operations for Australia had been in country recently; apparently he at the moment plans to cover Australian business from Manila, a long flight from Sydney. Department of Infrastructure and Transport General Manager for Aviation Markets Stephen Borthwick told econoff June 1

that he had signed off on the international airline licenses for Delta and Northwest (NW because it will be codesharing into Australia on Delta flights) last week, the final step in regulatory requirements for Delta. He said the GOA looked forward to Delta entering the Australia-California market.

18. (C) Virgin Blue's Wheelens said they had been in talks with Delta about codesharing and other commercial cooperation. Wheelens thought V Australia and Delta individually would be "vulnerable" to the Qantas American/United Air New Zealand duopoly, especially when considering the trans-Pacific market in US/Canada/Australia/New Zealand terms rather than just US-Australia. He noted the need for antitrust approval from the US DOJ and the Australian Competition and Consumer Commission (either AT immunity or something limited only to codesharing), but thought that would probably be granted given the dominant positions of United and Qantas/AA on the routes already. If forced to compete individually, Wheelens said he feared Delta and V Australia could fail, letting the Q said he feared Delta and V Australia could fail, letting the market revert to Qantas and United. In that instance, Wheelens (a former GOA civil official) opined, the GOA would probably allow Air Singapore and Emirates access to the Australia-US market - but the preference was to bolster Australian aviation, and Virgin Blue.

FAA ISSUES

18. (SBU) Wheelens raised one FAA issue - the ETOPS capability of the Boeing 777. Wheelens noted that an FAA recognition that the 777's ETOPS capability of 240 minutes is better than the current FAA limit of 180 minutes would be a big help for Virgin Blue. A decision to recognize the 240 minutes would save Virgin Blue money and allow them to carry more passengers on the Perth-Johannesburg segment by using Mauritius vice Diego Garcia, shortening the flight considerably.

19. (SBU) Qantas' McKeon expressed concern about the FAA

CANBERRA 00000511 003 OF 003

Reauthorization Bill before Congress. Specifically, she was concerned about the issue of having all antitrust immunity for alliances expire in three years and be subject to review.

The provision that would disallow the spraying of disinfectants on aircraft on flights to or from the US would be a real problem for Qantas, because the Australian Quarantine and Inspection Service requires it. Provisions to introduce drug and alcohol testing into foreign repair stations would on one level not hurt Qantas - they are already doing it - but could be an issue for them with their labor force. And finally, McKeon said Qantas was concerned about the proposed compensation for delayed bags, noting that the draft legislation doesn't distinguish between a bag delivered by the airline to the airport promptly and then delayed on the ground or a bag delayed by the airlines' own problems - either way, the airline would pay.

CLUNE